

## CREDIT OPINION

10 December 2020

### RATINGS

#### Bolzano, Autonomous Province of

Domicile	Italy
Long Term Rating	Baa1
Type	LT Issuer Rating - Dom Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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# Autonomous Province of Bolzano (Italy)

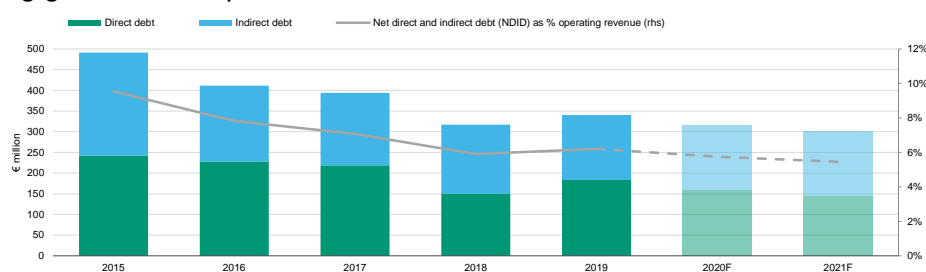
## Update to credit analysis

### Summary

The credit profile of the [Autonomous Province of Bolzano](#) (Bolzano, Baa1 stable) is underpinned by its (1) statutory independence, which provides a high degree of financial and legislative autonomy; (2) solid budgetary performance, which will buffer the negative fiscal pressure stemming from the Covid-19 pandemic; and (3) very low and declining debt. Bolzano's finances however remain exposed to nationally imposed budgetary restraints, sovereign credit conditions and economic downturns, such as the one triggered by the pandemics. Bolzano's credit profile is above that of the [Government of Italy](#) (Baa3 stable) because of its idiosyncratic features.

Exhibit 1

### Negligible debt level expected in the future



F = Forecasts

Sources: Issuer and Moody's Public Sector Europe

### Credit strengths

- » Long-established autonomous status
- » Budgetary performance resilient to Covid-19 impact
- » Negligible debt level

### Credit challenges

- » Wealthy and diversified economic base, challenged by the pandemics
- » The country's operating environment to challenge the region's superior financial flexibility

## Rating outlook

The stable rating outlook reflects our expectation of continued strong operating performance while debt levels will remain negligible.

## Factors that could lead to an upgrade

We would consider upgrading the rating of Bolzano if Italy's sovereign rating were upgraded.

## Factors that could lead to a downgrade

Although unlikely, any change in the province's unique status would strain its rating. Similarly, a growing exposure to indirect debt could also exert downward pressure on the rating, depending on the pace and sustainability of such growth. We would also consider downgrading the rating in case of a downgrade of Italy's sovereign rating.

## Key indicators

Exhibit 2

### Autonomous Province of Bolzano

Year ending December 31

	2017	2018	2019	2020F	2021F
Net direct and indirect debt as % of operating revenue (1)	7.1	5.9	6.2	5.8	5.5
Cash financing surplus (requirement) as % of total revenue	8.0	0.6	3.1	-	-
Gross operating balance as % of operating revenue	24.0	18.9	19.4	12.8	16.6
Interest payments as % of operating revenue	0.0	0.0	0.0	0.0	0.1
Intergovernmental transfers as a % of operating revenue	7.9	8.8	9.5	17.2	12.0
Capital spending as a % of total expenditure	27.2	21.5	26.4	22.2	23.8
GDP per capita as a % of national average	159.7	161.0	161.0	-	-

(1) Net direct and indirect debt figures include 1) direct debt, 2) a guarantee to ASSE, 3) a credit facility from the region.

F = Forecasts

Sources: Issuer and Moody's Public Sector Europe

## Detailed credit considerations

The credit profile of Bolzano, as expressed in its Baa1 stable rating, combines (1) a Baseline Credit Assessment (BCA) of baa1, and (2) a moderate likelihood of extraordinary support coming from the national government in the event the province faces acute liquidity stress.

### Baseline Credit Assessment

#### Long-established autonomous status

Bolzano is an autonomous province under the Italian framework and as such it can retain 90% of the revenue generated in its territory. The latest bilateral agreement with the central government (Patto di Garanzia, October 2014) reinforced Bolzano's legislative and financial autonomy. Bolzano has already modified the statute, reflecting its bilateral agreement with the central government, and the legislative protection significantly stabilises Bolzano's financial autonomy.

Under this agreement, the definition of national budgetary consolidation objectives in terms of cost-cutting and performance goals are now set on a bilateral basis and predefined objective parameters such as national GDP, which is credit positive for Bolzano. The agreement with the central government provides that Bolzano's contribution to public finance was equivalent to €451 million in 2019 and that until 2022 the central government can raise the contribution from Bolzano up to a yearly maximum of 10% (only in case of exceptional circumstances). From 2023, the province will renegotiate its annual contribution with the central government. As per this agreement, Bolzano must now only comply with the balanced-budget rule, which they have been complying with since 2012.

#### Budgetary performance resilient to Covid-19 impact

Bolzano has a consistent track record of very strong budgetary results. Because of its strong economic fundamentals, the province has historically generated solid operating revenue, which, along with effective spending-control mechanisms, has led to healthy operating

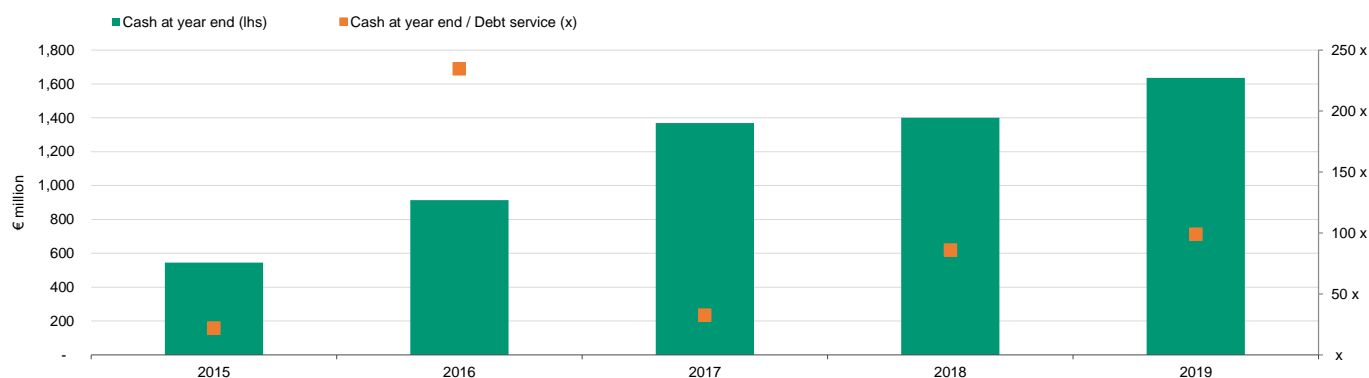
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surpluses of a very high 19% of operating revenue in 2019, slightly lower than the 24% posted in 2017 because of higher personnel and healthcare spending.

The ongoing pandemics will negatively impact Bolzano's budgetary results, although we expect this to be largely contained to 2020-21 period. Namely, in 2020 we forecast a decrease of around €430 million or 9% of tax revenues. However, this will be counterbalanced by ongoing central government support measures: a reduction of the 2020 contribution to public finance of €370 million, €50 million transfer granted through the special decree DL 104/2020 and €42 million to cover the provincial corporate income tax plunge. Factoring in a moderate increase in operating expenditure (personnel and healthcare), we forecast gross operating balance (GOB) at 13% of operating revenue in 2020. In 2021, we expect the regional economy to recover in line with the national one, while the operating expenses growth will slowdown. Therefore we foresee a GOB at around 17% of operating revenue.

Over the past five years, the province's capital spending activity has been high, averaging 27% of its total expenses, mainly comprising direct spending to develop the local economic landscape. So far, capital spending has not required material debt financing, and was rather funded through its strong operating performance, also supported by operating-efficiency measures. In 2019, Bolzano recorded an accrual financing surplus of €470 million, in line with its historical surpluses. We expect Bolzano to keep posting healthy yearly surpluses, which may however reduce with capital spending. Moreover, Bolzano can count on a comfortable liquidity position, with cash availability at €1.6 billion at YE2019 (covering 99x Bolzano's debt service) and registered at €1.9 billion in December 2020.

Exhibit 3

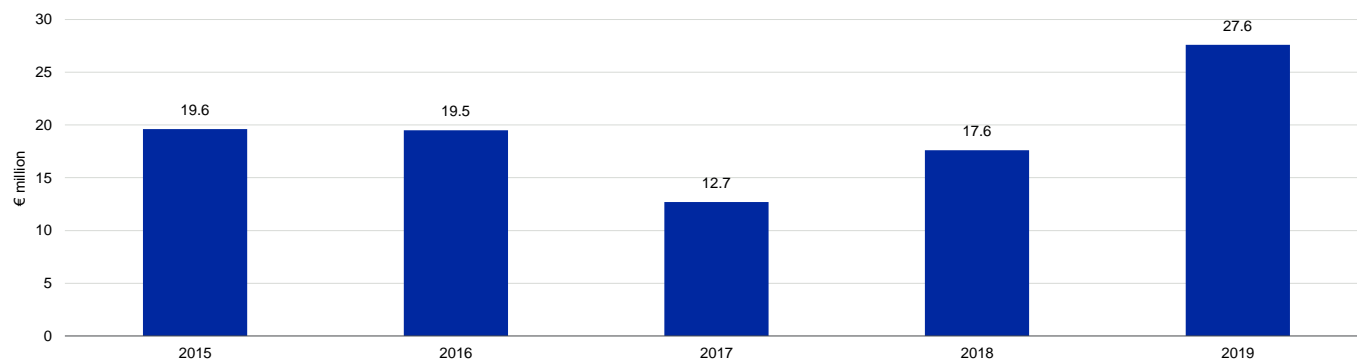
**Comfortable liquidity position**

Sources: Issuer and Moody's Public Sector Europe

In terms of spending, the province enjoys greater autonomy and greater spending flexibility than other Italian regions. Bolzano's spending is also more diversified, with healthcare accounting for just about 23% of the total compared with 75% for other regions or provinces. However, this greater flexibility is counterbalanced by greater commitments than that of other regions to the welfare sector and responsibility for supporting the local economy in a challenging environment.

Bolzano has an overall healthy and efficient healthcare sector by national standards, systematically posting surpluses. Because of its special statute, Bolzano's healthcare sector is wholly self-funded. Spending streamlining initiatives have helped curb the growth in healthcare costs and will continue, for instance, with the digitisation of its healthcare system. In 2020, in order to face the pandemics emergency, the healthcare sector exceptionally received €30 million from the central government and was transferred €70 million from the province to be spent in anti-Covid-19 screening activities and extra related equipment (€50 million) and civil protection (€20 million). These funding measures will ensure a healthcare sector surplus in 2020. On the long run, we however note that the cost of personnel will increase to attract bilingual professionals to replace future pensioners.

Exhibit 4

**Growing healthcare surplus**

Sources: Issuer and Moody's Public Sector Europe

**Negligible debt level**

Bolzano's net direct and indirect debt stock stood at around €340 million as of year-end 2019, equivalent to a very low 6.2% of realised operating revenue, marginally up from the 5.9% registered in 2018. In 2019, the net direct and indirect debt includes a €40 million loan, a guarantee to support its economic development agency (ASSE) for €156 million, and a credit facility from the region to support economic development for €144 million. We expect the province to slightly decline its debt level in 2020 to reach €316 million, or 5.5% of operating revenue, essentially on the back of a lower loan burden.

Bolzano is responsible for financing its municipalities and local public companies. It does so through a special funding called Fondo di Rotazione, which amounted to €332 million in 2019. However, given the low interest rate environment, the province decided to reincorporate these resources to its main budget starting 2020. We do not expect this to have a significant impact on the debt levels in the future.

**Wealthy and diversified economic base, challenged by the pandemics**

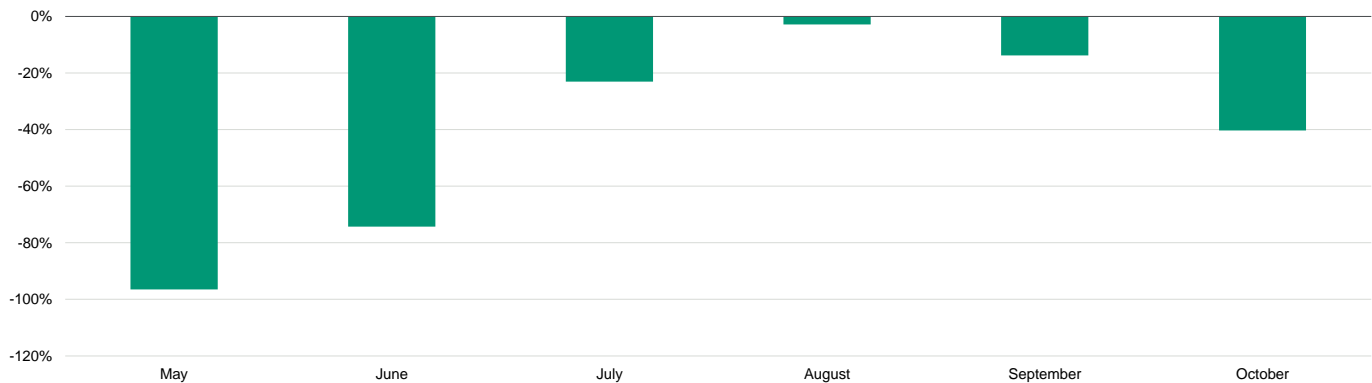
Located in the northeast of Italy, Bolzano has a small, but strong economy with a GDP per capita of around 61% above the national average. In 2020, the province's population has grown to 532,080 over the past few years and is younger, on an average, than the country's as a whole; 14.5% of local population is under 14 years versus 12% at the national scale. The population of the province is also driven by a strong birth rate (10.0 births out of 1,000 inhabitants) compared with the national average (7.3 births out of 1,000 inhabitants).

Bolzano's economy is essentially service driven, with the tertiary sector representing 71% of gross value added, followed by industry at 24% and agriculture at 5%. The service sector includes the provincial administration, which accounts for around 18% of the total gross value added. Tourism makes up 14% and is one of the key drivers of growth, together with exports. The dynamism of Bolzano's labour market is reflected in its low unemployment rate, which accounts for around one-third (2.9%) of the national unemployment rate of 10% in 2019. A solid economic growth is credit positive for the province as it drives fiscal revenue up in a larger scale compared with that in ordinary regions because of Bolzano's ability to retain 90% of its fiscal base.

Nonetheless, Covid-19 challenged the provincial economy through the limitations in exports and the drastic decrease in the number of tourists. Over the summer season, the number of tourists lowered on average by 34% with respect to the previous year (see Exhibit 6) and the winter season tourism will likely be undermined by lockdown measures, historically pivotal for the provincial economy. In 2020, Bolzano has intervened with supportive measures for around €270 million to support the local economy and is currently discussing with the central government for possible additional financing.

Exhibit 5

### Tourism undermined by Covid-19 impact 2020 vs 2019 monthly touristic presences



Sources: Issuer and Moody's Public Sector Europe

### The country's operating environment to challenge the region's superior financial flexibility

Italy's slowing economy and federal fiscal plan are likely to drive budgetary deficits higher, which will affect all regions, including Bolzano. We expect Bolzano's contribution to national austerity measures to be manageable in light of its excellent financials, tight budgetary control and efficient administration. We also note that Bolzano's contribution to national fiscal consolidation is highly predictable because of the bilateral agreement with the central government in 2014. That said, despite its unique constitutional status, the region is not completely insulated from the national operating environment.

In 2020 the province was able to use its previous years' cumulated surplus to fund current capital spending, given its greater flexibility, which is credit positive. We however note that capital spending keeps being constrained by complex administrative procedures.

### Extraordinary support considerations

We consider Bolzano to have a moderate likelihood of extraordinary support from the central government, reflecting the province's long-established special autonomous status.

## Environmental, social and governance (ESG) considerations

### How ESG risks inform our credit analysis of Bolzano

We take into account the impact of environmental (E), social (S), and governance (G) factors when assessing sub-sovereign issuers' economic and financial strength. In the case of Bolzano, the materiality of ESG to the credit profile is as follows:

Environmental considerations are not material to Bolzano's credit profile. Its main environmental risk exposures relate to its susceptibility to avalanche and landslide risks. Both are predominantly managed by national authorities, especially in case of emergency (*stato di emergenza*). Therefore the corresponding negative economic and fiscal pressure that could arise on Bolzano's credit profile is limited. Environmental risks are also mitigated by the strong coordination with the civil protection and the access to EU funds, which can be used in case of natural damages, while the province's capital spending aiming at preventing and reducing the impact of such events contains those risks.

Social risks are not material to Bolzano's credit profile. We view the coronavirus pandemic as a social risk under our framework, given the substantial implications for public health and safety. Exposure to social risks, associated to demographic, labour income and education, is potentially material as Bolzano is responsible for healthcare and social care services, while education is also an important cultural topic (bilingualism). Besides, as other autonomous Italian provinces and regions, Bolzano's credit profile is more exposed to economical cycle than ordinary regions. However, those risks are well managed, with the healthcare sector being structurally balanced while Bolzano's social pressures are limited with Bolzano's unemployment and poverty rates significantly below the national average.

Governance considerations are material to Bolzano's credit profile. Bolzano's governance and management are strong, its policies are credible and effective, with a good track record of sound financial results associated with high data transparency. Bolzano also benefits from a strong regulatory framework.

Further details are provided in the "Detailed credit considerations" section above. Our approach to ESG is explained in our cross-sector methodology [General Principles for Assessing ESG Risks](#).

## Rating methodology and scorecard factors

### Output of the BCA Scorecard

The assigned BCA of baa1 is one notch above the scorecard-indicated BCA. The matrix-generated BCA of baa2 reflects (1) an Idiosyncratic Risk score of 2 (presented below) on a 1-9 scale, where 1 is the strongest relative credit quality and 9 the weakest; and (2) a Systemic Risk score of Baa1. In the case of Bolzano, the Systemic Risk score of Baa1 exceeds the sovereign bond rating by two notches, which reflects its limited borrowing requirements, its constitutional protection and its outstanding financial flexibility, which could offset the impact of any sovereign decision detrimental to its financials.

For details about our rating approach, please refer to [Rating Methodology: Regional and Local Governments](#), 16 January 2018.

Exhibit 6

## Autonomous Province of Bolzano

## Regional and Local Governments

Baseline Credit Assessment	Score	Value	Sub-factor Weighting	Sub-factor Total	Factor Weighting	Total
<b>Scorecard</b>						
<b>Factor 1: Economic Fundamentals</b>				1	20%	0.20
Economic strength	1	160.81	70%			
Economic volatility	1		30%			
<b>Factor 2: Institutional Framework</b>				3	20%	0.60
Legislative background	5		50%			
Financial flexibility	1		50%			
				1.5	30%	0.45
<b>Factor 3: Financial Performance and Debt Profile</b>						
Gross operating balance / operating revenues (%)	1	19.91	12.5%			
Interest payments / operating revenues (%)	1		12.5%			
Liquidity	1		25%			
Net direct and indirect debt / operating revenues (%)	1	6.20	25%			
Short-term direct debt / total direct debt (%)	3	13.80	25%			
<b>Factor 4: Governance and Management - MAX</b>				1	30%	0.30
Risk controls and financial management	1					
Investment and debt management	1					
Transparency and disclosure	1					
<b>Idiosyncratic Risk Assessment</b>						1.55(2)
<b>Systemic Risk Assessment</b>						Baa1
<b>Suggested BCA</b>						baa2

Sources: Issuer and Moody's Public Sector Europe

## Ratings

Exhibit 7

Category	Moody's Rating
<b>BOLZANO, AUTONOMOUS PROVINCE OF</b>	
Outlook	Stable
Issuer Rating - Dom Curr	Baa1

Source: Moody's Investors Service

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